



**Investment Office**

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August 18, 2008

**AGENDA ITEM 5a**

**TO: MEMBERS OF THE INVESTMENT COMMITTEE**

- I. SUBJECT:** Investment and Diversification in Emerging Market Real Estate
- II. PROGRAM:** Real Estate
- III. RECOMMENDATION:** Information
- IV. ANALYSIS:**

On September 10, 2007, the Investment Committee (IC) approved the Strategic Plan ("Plan") for the CalPERS Real Estate portfolio, which contained a number of findings and recommendations to be implemented to the investment portfolio in the coming 5 to 10 years. One of the Plan's fundamental recommendations was to increase the real estate allocation and investment strategy to international markets. The Plan's discussion on international markets emphasized increasing emerging market exposure in real estate strategies that include sectors correlated with the emergence of the middle class such as housing, retail, logistics and infrastructure.

Investment staff jointly engaged the consultants of Pension Consulting Alliance, Inc. and PCA Real Estate Advisors, Inc. to provide an in-depth background briefing on international emerging markets. The assignment addressed topics of defining emerging markets, identifying markets that are emerging, historical performance of emerging markets, emerging market risks, and investment drivers of emerging markets such as demographics, GDP, financial transparency, capital flows (foreign direct investments), legal and political environments. The Real Estate Unit is proposing to use the FTSE definition of emerging markets which is the same definition used by Global Equities for emerging equity markets. The consultant's background briefing is included to this agenda as Attachment A.

In summary, the consultant's background briefing supplements the Plan's recommendation to increase exposure to emerging market real estate investments. On a long term basis, emerging markets are expected to outperform developed markets due to higher GDP growth, growing middle class demographics, urbanization trends and shifts toward manufacturing and service industries.

Attachment B illustrates the Real Estate portfolio on a percentage basis by geographic market as of March 31, 2008. Attachment C shows the real estate holdings by country, as of March 31, 2008, on an equity (NAV) basis in emerging and frontier markets.

Additionally, staff is proposing to revise its Statement of Investment Policy for International Equity Real Estate to define geographic markets (including emerging markets), delineate geographic diversification and establish investment guidelines and principals for responsible investing. This proposal will be presented at Policy Subcommittee meeting on August 18, 2008.

## **V. STRATEGIC PLAN:**

Implementation of the Real Estate Strategic Plan will further the following CalPERS Strategic Plan goals:

- Goal VIII. Manage the risk and volatility of assets and liabilities to ensure sufficient funds are available, first, to pay benefits and second, to minimize and stabilize contributions.
- Goal IX. Achieve long-term, sustainable, risk adjusted returns.

## **VI. RESULTS/COSTS:**

This item is provided for information only.

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